No. 14573

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

ELI B. CASTLEMAN, MARION V. CASTLEMAN, LOUIS FEUERMAN, JULIUS NOVEMBER, ELEANOR NOVEMBER, and BERNARD REICH,

Appellants,

vs.

HOWARD R. HUGHES, RKO PICTURES CORPORATION, RKO RADIO PICTURES, INC., THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, ELI B. CASTLEMAN, MARION V. CASTLEMAN and LOUIS FEUERMAN,

Appellees.

APPELLANTS' REPLY BRIEF.

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TOPICAL INDEX

TABLE OF AUTHORITIES CITED

CASES PAGE

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APPELLANTS' REPLY BRIEF.

Preliminary Comments.

We hope to be forgiven for what should be immediately obvious.

1. No brief for the Appellee Hughes has been filed.

The Appellee RKO argues that service of process on Mr. Hughes, having been quashed below, he is "not before this Court," losing sight of the principle that an appeal from a final judgment brings up for review intermediate

orders or matters. (Please see Appellants' Op. Br. p. 24, *et seq.*)

2. Appellees have restated the facts based on *their* affidavits, without challenging Appellants' statement of facts as based on the record made, losing sight of the principle that where an action has been summarily dismissed, the allegations in the record supporting Appellants must, for the purposes of the appeal, be taken as true.

3. Appellees seek affirmance predicated on the *discretion* of the trial court, losing sight of the principle that where the trial court refuses a trial, abdicates its jurisdiction and fails to exercise its discretion, the judgment may not stand. (Please see Appellants' Op. Br. p. 24, *et seq;* p. 31, *et seq.*)

4. The responsibility for the arrangement of the caption on appeal (erroneously challenged by Appellees) was the Clerk's, not ours.

5. The Appellees do not appear to have challenged a single law or fact citation set forth in Appellants' Opening Brief.

6. The New York attorneys' anger directed at plaintiffs' attorney of record stems from the latter's refusal to renounce his responsibilities to the Court as local counsel and his setting aside of the first dismissal entered by them without his knowledge or consent.

We would make one further preliminary comment, although it is perhaps less obvious than the others. The Appellee RKO, gently, and the Appellees Castleman and Feuerman, harshly, charge that plaintiffs' attorney of record has been motivated only by the question of fees,

losing sight of the fact that there are many lawyers who believe in the sanctity of their oath. [Please see Appellants' Op. Br., Appendix; also R. 371-373.]

We do, however, regret one thing: No matter how objective and unemotional we have aimed to be, we could not avoid the frequent use of the name of plaintiffs' attorney of record. We can only hope that the Court will be understanding of the problem which faced a lawyer trying in his perhaps inadequate way to maintain the responsibility and integrity of any local counsel, protect the interests of the stockholders, and yet keep in mind his obligations to his "trustee-clients."

Is it any wonder that this lawyer, turning to the District Court, asked [R. 373]:

> "Mr. Reich: Well, your Honor, what would you do about it? What could I do about it? You advise me and I will do it. I just want to do what is right. You tell me what to do and I will do it.
>
> The Court: I am not telling you what to do."

ARGUMENT.

I.

The Nevada State Judgment, Being Subject to Attack for Collusion, Etc., Is Not Res Judicata Until the Issue Is Tried in the Court Where It Is Legally and in Good Faith Raised.

The heading above is the very heart of the case and was treated at page 12, *et seq.,* of the Opening Brief.

Had the Court below tried the issue and found against the allegations, then the cases cited by Appellees would have had some applicability.

In *Masterson v. Pergament,* 203 F. 2d 315, 330, there was no opposition to the settlement, no proposed interveners, and no contention that the stockholders were not adequately represented.

In *Cohen v. Young,* 127 F. 2d 721, 724-725, there was a finding below of adequate representation. Nevertheless, on an appeal by a proposed intervener who had been denied intervention below, the judgment was reversed over the opposition, as herein, of the plaintiffs.

In *Winkelman v. General Motors Corporation,* 48 Fed. Supp. 490, it was indeed held that the trial court's role is to ferret out fraud and collusion. This is the role which the Court below should have assumed when the issue was raised before it. The fact that it was also the role of the Nevada court does not convert a duty into a fact, or preclude by any "boot-strap" argument the stockholders from challenging the entire Nevada proceeding as collusive.

In *Pergament v. Frazer,* 93 Fed. Supp. 13, 16, the action tried was the action first filed. All objecting

stockholders who appeared in other courts appeared here. The Court tried the issues of collusion and inadequate representation.

In *Stella v. Kaiser,* 218 F. 2d 64, one of the out-of-state stockholders in *Pergament v. Frazer, supra,* attempted to *retry* the issue of collusion in his own state.

In the instant case, the issues of collusion and inadequate representation were "tried" in Nevada as between the very parties charged with collusion and fraud. [R. 114.] Appellees' argument here amounts to this: "We, whose very actions are challenged, are not subject to attack in California because between ourselves we have resolved the issues in Nevada." Unlike in the *Stella* case, *supra,* no stockholder here attempted to *try* the issue of collusion in Nevada; and therefore again unlike *Stella,* no stockholder, including the Appellants November, has attempted to *retry* the issue of collusion in the Court below.

Moreover, the Appellants November were denied intervention in Nevada. They had the right to intervene here.

Pellegrino v. Nesbit, 203 F. 2d 463 (C. A. 9, 1953);

Cuthill v. Ortman-Miller Machine Company, 216 F. 2d 336 (C. A. 7, 1954);

Cohen v. Young, 127 F. 2d 721, 724-725 (C. C. A. 6, 1942).

Nierbo v. Bethlehem Shipbuilding Corp., 308 U. S. 165, cited by Appellees Castleman and Feuerman, was a venue case as between Federal district courts, with no allegation of collusion.

Kentucky National Gas Corporation v. Duggins, 165 F. 2d 1011, involved the law question of whether selection

of a forum constituted collusion. It was not a stockholder suit and the issue of collusion was tried.

E. B. Latham & Co. v. Mayfair Industries, Inc., 278 App. Div. (N. Y.) 90, and *Paramount Pictures v. Blumenthal,* 256 App. Div. (N. Y.) 756, involved similar suits in which plaintiff sought to enjoin a foreign court without alleging fraud. Moreover, they were not stockholder suits.

II.

No Stockholder or His Attorney Is Estopped From Challenging the Nevada State Judgment for Collusion (Except Possibly the Castlemans and Feuerman Personally).

It is true that the Novembers sought to intervene in Nevada; but their application was denied. It is true that if they had appealed, assuming the denial appealable, and had lost, they *might* have been bound by the Nevada judgment. We say *might* because it would depend on whether the issue of collusion was litigated. The fact is that the Novembers never litigated that issue in Nevada, as did the stockholder *Stella* in 218 F. 2d 64.

In the instant case, the District Court suggested that interveners apply to the Nevada state court. However, when the Novembers applied in Nevada their application was denied; *when they applied below their application was not ruled on.*

Please note that the court below did not rule that the Novembers were estopped to intervene herein by reason of the denial in Nevada.

Moreover, a representative action is not like any other action. Assuming, as we must, the truth of the allega-

tion of collusion in the Nevada action, including the intervention proceedings, the question, no matter how raised, must be considered by a court of competent jurisdiction. What better forum than in the court where the action was commenced prior to the challenged* Nevada action?

As to Reich being "a mere volunteer," we thought that that argument had been disposed of below when the District Court made no order of substitution or of dismissal for lack of prosecution, and when this Court denied the motion to dismiss the appeal.

We thought also that when Appellees failed to challenge the principles governing the duties and rights of an attorney in this kind of action, as set forth in Appellants' Opening Brief, pages 43 and 44, that Appellees would cease making the issues personal to the attorneys.

III.

The Nevada Judgment Did Not Meet the Requirements of Due Process.

Because the District Court refused to try the issue, the ultimate correctness of the above heading is really not before this Court. For example, Appellees' claim that the Novembers had notice of the Nevada "compromise" because they "appeared" by an attorney. This again flies in the face of the rule that the Novembers' allegations to the contrary must be assumed true. [R. 257-259.]

Moreover, without directly challenging the Opening Brief, page 17, demonstrating that the Nevada court converted a motion to dismiss for mootness, of which the

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*We make no charges against the Nevada court, as indeed we make no charges against the Court below. Our only point is that the Nevada judgment and orders were wrongfully procured.

stockholders had notice, to a 23(c) hearing, of which the stockholders had no notice, Appellees cite from their own evidence (in conflict with Appellants') to support their side of the issue. *But issue it is, and it has not yet been resolved.*

Nor are any of the Appellees' citations applicable. In *Mullane v. Central Hanover Bank & Trust Co.,* 339 U. S. 306, the Court held insufficient statutory constructive service under the New York Banking Law as applied to known beneficiaries.

Turner v. Alton Banking & Trust Co., 181 F. 2d 899, held that a "cognovit" note, *i.e.,* a note containing a warrant for an attorney's appearance, complied with due process.

IV.

Neither the Delaware Action nor the Sale to Appellee Hughes of All Assets Rendered the Action Herein Moot.

Appellees have failed to challenge the significance of a single authority cited by Appellants in support of the above heading. (Appellants' Op. Br. p. 19, *et seq.*) Instead they cite cases which we submit are inapplicable; although Appellees would have the Court read through the whole of each case to find, or rather *not* to find, their point.

For example, none of the cases cited by Appellee RKO on page 21 of its Brief holds, as suggested by it, that a sale to an officer or director of a corporation extinguishes the fraud claims against him. On the contrary, one case cited, *Webster Eisenhohr, Inc. v. Kalodner,* 145 F. 2d 316, 325, directly suggests the exact opposite; and two

other cases, *May v. Midwest Refining Co.,* 121 F. 2d 431, and *Malcolm v. Cities Service Co.,* 2 F. R. D. 405, indirectly suggest the same contrary conclusion.

The *May* case, *supra,* held that the statutory remedy of a dissenting stockholder was not exclusive; that the stockholder may maintain an equity action. However, where there are no interveners or other interested stockholders, the action may be treated as *non-representative,* and the stockholder may have his individual damages. (On the other hand, counsel fees were held not so restricted, the award being in excess of $40,000.00.)

The *Malcolm* case, *supra,* held that the sale by plaintiff of her stock to one of the defendants did not constitute a compromise and that (2 F. R. D. at p. 47): The cause of action, if there be one, remains unaffected by the sale of plaintiff's stock." The Court also held that other stockholders should be allowed to intervene to protect the action.

The cases cited by the other Appellees beginning on page 26 of their Brief fare even worse. None of them bears on the point at all. One deals with a classic example of mootness; another deals with a classic case of *res judicata,* and still others deal with situations where collusion is not an issue.

What Appellees have done here, and only in less degree throughout their Briefs, was condemned in *Lewis v. Manufacturers Casualty Insurance Co.,* 107 Fed. Supp. 465, 473-474, from which we quote but a single sentence: "This is legal fog."

V.

The Appeal From the Final Judgment Brings Up for Review Important Intermediate Matters.

Western Union v. United States & M. T. Co., 221 Fed. 545, 550, 551, 552 (C. C. A. 8, 1915);

Victor Talking Machine Co. v. George, 105 F. 2d 697, 699 (C. C. A. 3, 1939);

Skirvin v. Mesta, 141 F. 2d 668, 672 (C. C. A. 10, 1944).

In the *Western Union* case, *supra,* an appeal from an order affecting a petition in intervention in a foreclosure suit alleging fraudulent transfers by bondholders and stockholders of an insolvent corporation, the Court stated (221 Fed at p. 551):

> "When a final order or decree is made in a proceeding in equity all the preceding interlocutory orders and decrees relative to the matters in controversy between the parties to the final order remain under the control and subject to the revision of the court, and upon an appeal from the final order or decree every interlocutory order affecting the rights of the parties regarding the matters in question between them is subject to review in the appellate court and may be heard and decided at the same time."

What was said of some of the intermediate matters before the district court there is most appropriate here. Said the Eighth Circuit Court (221 Fed. at p. 550):

> "Hence, laying aside the other alleged grounds of equitable relief set forth in the portions of the petition excised, which may be more wisely and satisfactorily considered after, at a hearing, the relevant facts have been definitely ascertained, *the averments*

> *of the cause of action invoked the undoubted power and duty of that court to hear and determine the issues* tendered thereby on their merits, a power and duty which it might not lawfully renounce or avoid; for 'the courts of the United States are bound to proceed to judgment, and to afford redress to suitors before them in every case to which their jurisdiction extends. *They cannot abdicate their authority or duty in any case in favor of another jurisdiction.*'" (Emphasis added.)

Also at page 552:

> "Moreover, there is a class of cases in which a party has the equitable right to intervene, and the right to review by appeal any order denying that right, and this case is of that class."

Some of the intermediate matters which we ask this Court to review are:

1. Motion to intervene (involved in the *Western Union* case, *supra*);

2. The order quashing service on Mr. Hughes (no opposition here by this Appellee);

3. Motion to set aside default on Mr. Hughes' motion to quash on grounds of fraud (no opposition here by this Appellee);

4. Motion for appointment of a Special Master.

Had these matters been disposed of favorably to Appellants, the Court below would have been in position to hear the evidence and may not have abdicated its jurisdiction (also involved in the *Western Union* case, *supra*).

Yet Appellees dismiss this important phase of the appeal by an unsupported general reference to a rule that such

omissions do not warrant reversal in the absence of prejudice or abuse of discretion.

We submit that the general principle thus invoked does not apply to situations where the trial court declines to *use* discretion; a point covered beginning on page 24 of our Opening Brief, and which the Appellees leave unchallenged.*

We take it that the Appellees would disagree with *Cuthill v. Ortman-Miller Machine Company,* 216 F. 2d 336, 338, 339 (C. A. 7, 1954), citing this Court's decision in *Pellegrino v. Nesbit,* 203 F. 2d 463 (1953).

In the *Cuthill* case, *supra,* the District Court had denied a stockholder's motion to intervene. On appeal the Seventh Circuit Court stated (p. 338):

> "Rule 24(a) of the Federal Rules of Civil Procedure, 28 U. S. C. A. provides that upon timely application one shall be permitted to intervene (a) when the 'representation of the applicant's interest by existing parties' is inadequate and the applicant is or may be bound by a judgment in the action, or (b) when the applicant 'is so situated as to be adversely affected by' disposition of property in the custody or control of the court or an officer thereof. Comparing the mandatory provisions of the rule with the averments of appellant's petition, it is obvious that he has brought himself within the rule by charging explicitly that as a stockholder he had a substantial interest in the $4,100 then in the custody of the court; that the corporation's interests, including appellant's, were not

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*Appellees Castleman, *et ano,* by taking words out of context and misunderstanding our courtesy to the Court below, attempt to blame the District Court's inaction on us, but please see the full text [R. 44-55, 80-91, 135-172].

adequately represented in that the company and its counsel had permitted a fraudulent judgment to be entered; and that if corporate funds were improperly diverted in satisfaction of the allegedly fraudulent judgment, his interests would be adversely affected. In this situation the court could not properly do otherwise than permit him to present his case. Thus, in Pellegrino v. Nesbit, 9 Cir., 203 F. 2d 463, at page 465, the court said: 'Intervention should be allowed even after a final judgment where it is necessary to preserve some right which cannot otherwise be protected.' . . .

"The facts pleaded were sufficient to justify appellant's fears; they brought him within the doctrine enunciated by the Supreme Court in United States v. Throckmorton, 98 U. S. 61, at page 65, 25 L. Ed. 93, where the court said: 'Where the unsuccessful party has been prevented from exhibiting fully his case by fraud or deception practiced on him by his opponent as by keeping him away from court, a false promise of a compromise; or where the defendant never had knowledge of the suit, being kept in ignorance by the acts of the plaintiff; or where an attorney fraudulently or without authority assumes to represent a party and connives at his defeat; or where the attorney regularly employed corruptly sells out his client's interest to the other side,—these, *and similar cases which show that there has never been a real contest in the trial or hearing of the case,* are reasons for which a new suit may be sustained to set aside and annul the former judgment or decree, and open the case for a new and fair hearing.' Citing cases. See also U. S. v. Kusche, D. C. 56 F. Supp. 201, at page 216. Here appellant pleaded with particularity and great detail facts tending to show that there had been *no adversary trial of the issue in the case; that this situation emanated from the*

collusion of the original parties; that appellant's interests were adversely affected and *that no adequate representation of his and the corporate interests had been supplied. Inasmuch as Rule 60(b) endows the court with power to vacate any fradulent judgment, plaintiff was entitled to be heard upon his averments.* Obviously the District Court has inherent power to investigate such averments of fraud. Hazel-Atlas Co. v. Hartford Empire Co., 322 U. S. 238, 64 S. Ct. 997, 88 L. Ed. 1250; Universal Oil Products Co. v. Root Refining Co., 328 U. S. 575, 66 S. Ct. 1176, 90 L. Ed. 1447." (Emphasis added.)

VI.

Counsel Fees Can Be Assessed Against Appellee RKO.

Again Appellees do not challenge or even discuss Appellants' citations in their Opening Brief beginning at page 42. Their entire defense is predicated on what the Nevada state court did or did not do.

In the first place, what the Nevada court did or did not do is challenged here and as yet has not been resolved by trial.

In the second place, counsel was entitled to have his fees fixed by the court below, the Appellees' cases on this point being inapplicable.

In each of the cases cited by Appellee RKO on page 26 of its Brief, and by the Appellees Castelman, *et ano,* on page 38 of their Brief, while it was held that the trial court could in a single jurisdiction fix fees for out-of-state attorneys, *those attorneys made application therefor and submitted themselves to that single jurisdiction.*

In each such case objection was made to the court's power to award fees to out-of-state attorneys. In the

instant case, Reich made no application in Nevada. His application was to the Court below, where he had rendered the services which he alleges brought about the offer on the part of Hughes to purchase the assets of RKO.

The fact is that the Court below did not exercise its discretion to award or not to award fees. He denied relief by declining jurisdiction on the ground of the *res judicata* of the Nevada state court judgment—without trying the issues of fraud and collusion.

One last thing on this point: the Appellees, without mention of the legal consequences therefor, refer to a stipulation staying proceedings, except for the deposition of Mr. Hughes, pending the outcome of the security application. Obviously, the stipulation failed when the deposition was not given, when the action was dismissed the first time without the knowledge or consent of plaintiffs' attorney of record, and in any event in the face of the collusion charges.

VII.

Counsel Fees Can Be Assessed Against the Appellees Castelman and Feuerman.

These Appellees negative the above heading by claiming that the Court below "did not abuse his discretion," when our point is simply that the Court below did not *use* or *exercise* its discretion.

These Appellees also base their defense on an assumption that the purported discharge was for cause and that the Court below so held. There was of course no such holding; the Court refused to rule. In fact, the clear inference from the Court's refusal to rule or grant the motion for substitution is that Reich had the right to

proceed in the case. In any event counsel was entitled to a hearing on the issue of the purported discharge and whether it was for cause.

It is significant that there was no cause for discharge—only confirmation of the retainer—until counsel successfully moved to set aside the first dismissal. [R. 276-278.] Appellees having been thwarted in their sordid undertaking, they attack counsel.

As to these Appellees' point that their attorney of record, having been "discharged," could not proceed in the case, there is not one word by Appellees in contradiction of the Opening Brief, pages 40 and 41, citing authorities that counsel's procedure was eminently correct; and that, under the rules of the court below, until there has been a substitution the attorney of record has the exclusive right to appear.

Instead of meeting the issues directly, these Appellees again cite inapplicable cases.

In *Thomas v. Thomas,* 34 N. Y. S. 2d 320, a divorce case, it was held that an *opponent* by reason of statute could not serve a discharged attorney. In the instant case, the opponent, *i.e.,* the Appellee RKO, continued to serve the "discharged" attorney of record, as indeed it should have.

In *Mueseler's Estate,* 220 P. 2d 18, it was held that a written dismissal of attorneys and waiver of appeal by a *legatee* was effective to nullify a notice of appeal—where there was a finding below of *no* fraud.

In *Margaretten v. Horowitz,* 112 N. Y. S. 2d 24, the Court denied an application for counsel fees made four years after a settlement and the filing of a dismissal without costs. Moreover, no fraud was alleged.

Conclusion.

Appellee RKO presses us to state what we propose to litigate in the event of a reversal.

If the judgment is reversed we propose to prosecute the case and endeavor to obtain a judgment of $38,000,000.00. If, on the other hand, the court below, on application of the defendants, wants to treat the "sale" to Hughes as an offer of compromise and to submit same to the stockholders, we shall petition for a full and complete hearing suggested by Circuit Court Judge Biggs,* at which time—and for the first time—all of the stockholders, and not just plaintiffs, will have notice that what is proposed is not a dismissal of the action on the merits, but a settlement of the lawsuit. The court below then, for the first time, will be in a position to approve or disapprove the settlement.

The judgment should be reversed in accordance with the prayer in Appellants' Opening Brief.

Dated: June, 1955.

Respectfully submitted,

BERNARD REICH,

Attorney for Appellants.

KENNETH N. CHANTRY,

Of Counsel.

**Webster Eisenhohr, Inc. v. Kalodner,* 145 F. 2d 316, 325 (C. C. A. 3, 1944).